

TESTIMONY OF

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Before the

*House Government Reform Subcommittee
Government Management, Finance, and Accountability*

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Thank you Chairman Platts, Congressman Towns, and members of the Subcommittee for asking the New York State Banking Department to report on the current status of financial market preparedness for wide-scale disasters or disruptions.

The New York State Banking Department is the regulator of more than 3,400 financial companies operating in New York State. This number includes 165 state chartered commercial banks and thrift institutions and 111 U.S. branches and agencies of foreign banks. The aggregate assets of these supervised entities total nearly \$1.3 trillion. The Department also licenses, supervises and regulates a total of 3,100 mortgage bankers, mortgage brokers, check cashers, money transmitters, licensed lenders and budget planners.

Since the tragic events of 9/11, the financial services sector has been on a steady march of progress towards strengthening its preparedness for disasters. The resiliency demonstrated after 9/11 and the August 2003 power blackout in the northeastern United States and Canada was truly remarkable, however we cannot afford to be complacent and I do not believe we have become so. If there was a threat of complacency setting in, the recent catastrophe in the Gulf Coast and New Orleans caused by Hurricane Katrina should serve as a horrible reminder of the need for continuing emphasis and attention to business continuity planning and testing. One thing is certain, it is impossible to be too prepared.

Coping with wide-scale disasters or disruptions, whether man-made or acts of nature, will always be difficult as the destruction that ensues taxes societies' normal expectations of public health and safety and order. Financial services providers do not after all live in a vacuum. They are your neighbors, they have families. The first rule in any disaster contingency plan is to provide for one's own safety and that of one's family. Business recovery plans come second and must account for the safety of employees and data simultaneously. At the local level, first responder agencies are critical to personal and business survival, rescue and recovery and need Congress's support. While much has been done to better supply and support local disaster teams, more emphasis on this critical function is needed.

Putting the health and safety issues aside, the Banking Department believes much progress has been made in disaster planning by the financial services sector. Systemically critical organizations have made substantial progress in improving their resilience and achieving out-of-region geographic dispersion between primary and backup facilities. These organizations are being held to a high standard of business resumption capability. All banking organizations are expected to maintain a level of resilience appropriate to their role in the marketplace.

The Banking Department believes that Congress can be of most assistance to the financial sector by supporting efforts to improve the resiliency of the power, water, transportation and telecommunications infrastructure upon which the financial sector relies.

The Banking Department plays an important role in assuring the banking industry in New York State is ready and prepared.

First, our most important function during an emergency is to act as a conduit of accurate information to state and federal senior policy and emergency officials about the status of the industry. To do this efficiently, we are an active participant in disaster recovery efforts on the local, state and federal levels. On the local level, we communicate and coordinate with the NYC Office of Emergency Management (“OEM”) and have established communication protocols. In the event of a disruption in New York City, as part of the Banking Department contingency plan, a senior member of our staff is assigned to NYC’s OEM operations center.

On the state level, the Banking Department is a member of the Disaster Preparedness Commission and coordinates activities with the State Emergency Management Office (“SEMO”). Banking Department staff regularly participates as needed in contingency drills conducted by SEMO. The Banking Department’s contingency plan includes assigning staff to the SEMO operations center in the event of a disruption in NYS.

Immediately after a disruption, it is our protocol to consult with the Governor’s office to assess the situation and to request an Executive Order declaring a bank emergency or holiday if necessary. Working with SEMO and our fellow federal regulators, we help deliver emergency services to affected institutions, assist in the delivery of cash or other needed banking services, answer consumer inquiries and advise the Governor’s office on the status of our financial institutions.

On the federal level, the Banking Department, working through the Conference of State Bank Supervisors, is an active participant in the Financial and Banking Information Infrastructure Committee (“FBIIC”) which has established a protocol that facilitates the sharing of information among the federal financial regulatory agencies, state financial regulators and others responsible for promoting the financial integrity and soundness of the financial services industry. FBIIC is chaired by the Department of the Treasury. Senior Department staff regularly attends FBIIC meetings and supports FBIIC efforts as needed. These protocols have proved valuable even in the events that have not directly affected New York State. For example, earlier this month we responded to a request for a public communications expert to assist the state of Mississippi which had been circulated through FEMA and SEMO. In addition, Department personnel are staffing a Harlem facility opened by OEM to assist Hurricane Katrina relocatees.

Secondly, through our regular on-site examination program for all our regulated entities, we are actively monitoring the status of business continuity plans and readiness at our regulated institutions. Department examiners use the Business Continuity Planning IT Examination Handbook issued by the Federal Financial Institutions Examination Council (FFIEC) when conducting such examinations and reviews. The examination procedures are designed to determine whether the institution has an appropriate enterprise-wide

business continuity plan that covers all business units and functions and that it is kept current and frequently updated. Examiners are instructed to determine:

- the quality of oversight and support provided by the Board of Directors and senior management;
- if adequate business impact analysis and risk assessment have been completed;
- if appropriate risk management over the business continuity process is in place;
- whether the plan includes appropriate levels and frequency of testing;
- whether the IT Business Continuity Plan properly supports the goals and priorities of the overall business unit plan;
- whether the appropriate hardware backup and recovery is maintained;
- whether the process includes appropriate data and application software backup and recovery;
- whether the plan includes appropriate preparation to ensure the data center recovery processes will work as intended;
- that the appropriate security procedures are included in the plan; and
- whether the plan addresses critical outsourced activities.

Examination findings and recommendations are formally communicated to senior management and if appropriate the Board of Directors. Corrective action plans are monitored by our examiners until resolved. If necessary, informal and in rare instances formal enforcement actions are taken to address serious deficiencies.

Results of the latest cycle of on-site examinations are satisfactory. While not every institution's business continuity plan meets all the supervisory expectations, the vast majority of institutions have developed adequate plans and/or are in the process of correcting deficiencies. Weaknesses most frequently cited by examiners relate to insufficient testing both as to coverage and frequency and inadequate independent audit or verification of test results. In a small number of non-critical institutions the plans are simply not comprehensive enough.

Critical and significant institutions have made significant strides in obtaining geographic diversity for critical functions. For many non-critical institutions primary and back-up sites tend to be within a relatively limited geographic area that could conceivably be simultaneously affected by a large-scale event. While this could hinder the speed of

business resumption and recovery for these institutions, it does not pose a systemic risk to the financial system and is considered adequate under the current supervisory standards and reflects a reasonable risk and cost-benefit analysis. We mention this simply to note that it is, of course, still possible that some institutions and their customers in individual cases could be inconvenienced in the aftermath of an event of significant force and geographic reach.

In conclusion, the Department is committed to ensuring that the institutions it supervises are as prepared as possible. We will continue to work with local, state, and federal agencies to seek practical solutions. We fully understand that business continuity planning is a continuous process that requires our constant vigilance and attention. This is best achieved through our on-going examination and supervisory process.